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OCT 20 1994

FEDERAL COMMUNICATIONS COMMISSION  
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October 20, 1994

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**EX PARTE**

DOCKET FILE COPY ORIGINAL

William F. Caton  
Acting Secretary  
Federal Communications Commission  
1919 M Street, N.W.  
Washington, D.C. 20554

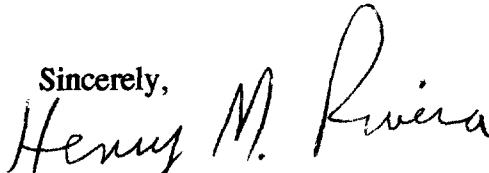
Re: PP Docket No. 93-253  
Implementation of Section 309(j)  
of the Communications Act - Competitive Bidding

Dear Mr. Caton:

On Thursday, October 20, 1994, a copy of the attached letter was delivered to Sara F. Seidman, Special Counsel, General Counsel's Office.

Two copies of this letter are being submitted to the Secretary of the Commission pursuant to § 1.1206(a)(1) of the Commission's Rules.

Please contact the undersigned if you have any questions or require additional information concerning this matter.

Sincerely,  
  
Henry M. Rivera

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**EX PARTE**

Sara F. Seidman  
General Counsel's Office  
Federal Communications Commission  
1919 M Street, N.W.  
Washington, D.C. 20554

Re: PP Docket No. 93-253  
Implementation of Section 309(j)  
of the Communications Act - Competitive Bidding

Dear Ms. Seidman:

Pursuant to your telephone calls with Darren Nunn, we are submitting, on behalf of our client, Metricom, Inc., this proposal designed to deal with the concept of "control groups" as that concept relates to publicly traded companies. Pursuant to Rule § 1.1206, we have submitted a copy of this letter for inclusion in the record of the above referenced proceeding.

**Summary**

Metricom is a nine-year old company that has developed new and innovative technologies with application in the field of wireless data communications. Metricom is widely acknowledged as being on the leading edge of wireless telecommunications solutions, but

remains a relatively small company by communications industry standards, with calendar 1993 revenues of only \$10.1 million. As such, Metricom fits what must be the typical profile of publicly-traded small business applicants that Congress and the Commission want to take part in the PCS auction as a designated small business entity.

The purpose of this letter is to provide a solution to a perceived flaw in the rules adopted in the Commission in its Fifth Report and Order, PP Docket No. 93-253, FCC 94-178, Released July 15, 1994 (the "Fifth Report and Order") and the Second Memorandum Opinion and Order, PP Docket No. 93-253, FCC 94-215, Released August 15, 1994 ("the Second Memorandum Opinion and Order") adopting rules for PCS license auction (the "Final Rules"). Metricom believes that in the absence of modifications such as those proposed here the application of the Final Rules will significantly frustrate the intent of Congress and the Commission to foster a diversity of PCS licensees and "ensure that small businesses . . . are given the opportunity to participate in the provision of spectrum-based services."

Specifically, Metricom believes that the Final Rules will render thousands of businesses (that would be considered "small" by any objective standards) ineligible to bid for the so-called "entrepreneurs' blocks" and to receive the preferential treatment reserved for "small businesses."<sup>1</sup> Though the Commission's goal to prevent large corporations from receiving undue preferential treatment by using small businesses as a front is laudable, the method the Commission has adopted to achieve this goal will result in harm to some of the very entities the Commission seeks to help.

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<sup>1</sup>Metricom does not discuss in this Presentation issues specifically regarding minority/women-owned businesses and rural telephone companies.

The problem lies foremost in the tests set out for establishing whether a corporation is eligible to apply for licenses in the so-called "entrepreneurs' blocks'" (frequency blocks C and F), and whether it qualifies for preference as a "small business." The attribution rules established by the Commission for these purposes construct what appears to be an unnecessary, unintended and inappropriate barrier to small, publicly-traded companies' participation in the auction, as well as to their qualification for "small business" status. The attribution rule--and, in particular, the necessity of identifying a "control group" of shareholders--is entirely unworkable for many publicly-traded companies, where the actual control group may not in reality have a large ownership stake in the company.

Metricom proposes as a solution to the problem that, for purposes of its attribution and affiliate rules, the Commission recognize the existence of a *bona fide* alternative to the presence of a "control group" of shareholders in instances where the voting stock of a publicly-traded corporation is truly dispersed (*e.g.*, where no person or group of persons acting in concert holds more than 15% of the voting power of the corporation) and *de facto* control resides in management. The Commission can accomplish this by amending the present rules to incorporate the concept of "dispersed voting power" as outlined below and specified in Exhibit A attached hereto.

### **Background**

In enacting the legislation authorizing the use of competitive bidding procedures to award spectrum licenses, Congress directed the Commission to "ensure that small businesses, rural telephone companies, and businesses owned by members of minority groups and women are

given the opportunity to participate in the provision of spectrum-based services." 47 U.S.C. §309(j)(4)(D). To satisfy these Congressional mandates and objectives, the Commission established, in the Fifth Report and Order ¶65 "a menu of preferences . . . designed to ensure that small businesses, rural telephone companies, and businesses owned by members of minority groups and women (collectively, 'designated entities') are given the opportunity to participate in both the competitive bidding process and in the provision of spectrum-based services." Second Report and Order.

These provisions, as applied to the planned auction of PCS licenses, were revised and extended in the Fifth Report and Order, which also established the "entrepreneurs' blocks," the bidding for which would be restricted to relatively small "entrepreneurial businesses."

The rules dealing with the determination of an applicant's or licensee's size for purposes of the "entrepreneurial business" and "small business" categories, are based on Small Business Administration ("SBA") regulations. The SBA has examined the meaning of the term "small business" for over 40 years.

#### **Definition of "Entrepreneurial Businesses" and "Small Businesses"**

The Commission determined in the Fifth Report and Order that "entrepreneurial business" status would be limited to applicants, including publicly traded corporations, with less than \$125 million in annual gross revenues in each of the two previous years and less than \$500 million in total assets. 47 C.F.R. §24.709. The Commission also adopted rules that permit an applicant, including a publicly traded corporation to qualify as a "small business" so long as it satisfied the four requirements of the applicable definition, including the requirement that its

annual revenues for the preceding three years not exceed \$40 million after aggregating with its own revenues the revenues of all "attributable" investors and affiliates. 47 C.F.R. §24.720(b). The Commission's policy in each instance, which Metricom believes is consistent with Congress' intent, appears to be that publicly traded corporations can qualify to participate in the PCS auctions as an "entrepreneurial business" and be treated for these purposes as a "small business" so long as they are truly "small."

### **Reasons for Proposed Changes**

Metricom believes the Final Rules fail to give full effect to Congress' mandate regarding small businesses by unduly favoring privately held small businesses over publicly traded small businesses. There is no evidence in the legislation authorizing the competitive bidding process or in its legislative history that Congress intended publicly traded corporations that otherwise qualify as "small" to be disadvantaged in the bidding process relative to similarly-situated non-publicly traded businesses. Nor does the record in this matter reflect a determination by the Commission that all publicly traded corporations should be excluded from bidding for the "entrepreneurs' blocks." *See, e.g.,* Fifth Report and Order at ¶163. If Congress or the Commission had intended to exclude every publicly traded corporation from eligibility for "small business" status simply because of its publicly traded status, both would have done so directly and unequivocally. They did not.

On the contrary, both Congress and the Commission have properly focused on an entity's *size*, not the source of its capital, as the relevant criterion. In that vein, the Commission has adopted rules intended to prevent manipulation of "small" entities by larger ones that would

defeat the purpose of the preferences accorded the small entities by the Commission. Metricom submits that these rules, while fair and effective in many applications, are flawed in their application to small publicly traded corporations.

Consistent with the SBA rules, the Final Rules include an "affiliation" rule providing that, in applying the size tests for entrepreneurial and small businesses, an applicant or licensee must aggregate with its own revenues and assets the revenues and assets of its "affiliates," as defined in the Final Rules. 47 C.F.R. §24.709(a)(1).<sup>2</sup> The affiliation provisions of the Final Rules, which are patterned after the corresponding rules of the SBA, are "intended to prevent entities that, for all practical purposes, do not meet [the] size standards from receiving benefits targeted to smaller entities." Fifth Report and Order at ¶201.

Going beyond any concept embodied in the SBA rules regarding "small businesses," the Commission also adopted an "attribution" rule providing that, subject only to four specific exceptions, an applicant or licensee must also aggregate with its own revenues and assets the revenues and assets of *all* "persons that hold interests in the applicant (or licensee)," whether or not such persons would be considered "affiliates" of the applicant or licensee. 47 C.F.R. §24.709(b)(1). Of the four exceptions to this rule, one pertains to formation of a consortium of small businesses and is outside the scope of this submission; each of the other three requires a corporate applicant or licensee to identify a "control group" of shareholders who hold in aggregate at least 50.1% of the company's "voting interests" or "voting stock." 47 C.F.R.

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<sup>2</sup>Under the Final Rules, as in the SBA rules, two parties are generally "affiliates" of one another when one controls or has the power to control the other, both are controlled by the same third party, or there exists an "identity of interest" between them. 47 C.F.R. §24.720(l)(1) and 13 C.F.R. §121.401(a)(2).

§24.709(b)(4). One of these three exceptions applies to the definition of "entrepreneurial business," but not to the definition of "small business."

As a practical matter, this attribution rule renders ineligible for "entrepreneurial business" status every publicly-traded corporation whose voting stock ownership is dispersed enough to make it impracticable to identify a "control group" of shareholders who hold 50.1% of the corporation's voting stock as contemplated by the Final Rules. There are thousands of such corporations with less than \$125 million in annual revenues and less than \$500 million in total assets.<sup>3</sup> Metricom believes it was not the Commission's intent that these companies be denied the opportunity to bid on the entrepreneurs' blocks.

Similarly, the definition of "small business" in the Final Rules excludes from eligibility thousands of publicly traded corporations that would otherwise qualify as "small businesses" but for their inability to identify a "control group" within the meaning of the Final Rules given the wide dispersion of ownership of their voting stock. The Fifth Report and Order contains little explanation for the extraordinarily restrictive attribution rule applicable to publicly-traded corporations for purposes of the "small business" definition. This is especially puzzling in light of the Commission's acknowledgment that "these attribution rules may impose a particular hardship on publicly traded companies, which have little control over the ownership of their stock, and whose voting stock is typically widely held." Fifth Report and Order at ¶163. The only apparent explanation offered is that the Commission "[does] not believe . . . that publicly

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<sup>3</sup> As of October 18, 1994, not counting affiliates or attributable investors, there are over 5,000 publicly-traded companies that qualify under the less than \$125 million in annual gross revenues/\$500 million in total assets test set by the Commission for "entrepreneurial business" status. Of those, over 3,000 also meet the less than \$40 million in annual gross revenues to qualify as "small business." Standard & Poors database.



traded corporations with individual shareholders owning up to 15 percent active equity require additional special provisions . . . to overcome capital access problems." Fifth Report and Order at Footnote 141.<sup>4</sup>

The flaw in the Final Rules lies not in the explicit language of the rules, but rather in the practical effect of those rules in real world applications. Specifically, the problem is the requirement that all companies seeking "entrepreneurial business" or "small business" status identify a "control group" of shareholders holding a majority of the company's voting interests.

The purpose of the "control group" requirement is clear and commendable.<sup>5</sup> Unfortunately, the requirement is inconsistent with the realities experienced by publicly-traded corporations, which, as the Commission has acknowledged, typically have no influence over--or even knowledge of--the composition of their shareholder groups. Virtually all large, publicly-traded corporations, and a significant number of small ones, have voting share ownership that is sufficiently dispersed that, quite literally, no identifiable "control group" of shareholders exists or can be created. Such companies, regardless of size or access to capital, are absolutely

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<sup>4</sup>Footnote 141 appears to assume that a publicly traded company, even if small, has access to satisfactory sources of capital. However, the fact that a company has publicly traded stock does not guarantee that there is a robust public market for it to acquire new and sufficient capital, particularly in a business focused on exploiting new and unproven technologies in competition with some of America's largest corporations. Therefore, as a small business, regardless of the nature of its stockholders, the need for capital and some preference vis a vis large corporations still holds true. As the Commission noted, "small business . . . have not become major participants in the telecommunications industry." *Id.* at ¶108. Thus, to best promote diversity of license holders in the PCS auction, small businesses that happen to be publicly traded rather than privately held companies should not for that reason be denied the same opportunities.

<sup>5</sup>"Our attribution rules are designed to preserve control of the applicant by eligible entities, yet allow investment in the applicant by entities that do not meet the size restrictions in our rules." Fifth Report and Order at ¶205.

precluded by the Final Rules from bidding in the "entrepreneurs' blocks" or receiving the benefits accorded "small businesses."

The Commission indeed has recognized that a public corporation may be unable to identify a control group by applying the voting power rule: "voting control does not always assure *de facto* control . . . when the voting stock of the control group is widely dispersed." Note to 47 C.F.R. §24.720(k). Moreover, the Commission has acknowledged that management is considered to exert control over corporations where voting power is widely dispersed and no officer or director has, or all officers and directors as a group have, a voting interest equal to or greater than 50.1 percent of the corporation's voting stock. Example following 47 C.F.R. §24.720(l)(iii). Despite recognition of this inherent problem for small, publicly traded companies, no alternative test has yet been incorporated into the Commission's rules to assess control for purposes of determining attributable investors and affiliates.

This result, though harsh, might nevertheless be acceptable if it were necessary in order to achieve the underlying objective of the rules. However, the "control group" requirement is significantly broader than necessary for the accomplishment of the stated regulatory objectives of the attribution and aggregation provisions, namely, to prevent abuses involving large entities effectively masquerading as smaller ones and thereby gaining benefits intended only for small businesses, while simultaneously permitting smaller entities to obtain investment capital from entities that do not meet the applicable size restrictions. Second Memorandum Opinion and Order at ¶88 and ¶91.

The "control group" concept represents a creative and effective approach to balance the inherent tension between these two objectives. However, Metricom respectfully submits that the

Commission went farther than necessary when it established that concept as the *sole* method of avoiding aggregation of non-affiliate shareholders' revenues and assets for purposes of the size restrictions. In fact, it should be sufficient for the achievement of the stated regulatory objectives to require, as an alternative to satisfaction of the "control group" test, that the applicant or licensee *not* be controlled or significantly influenced by another entity (as would generally be the case in a situation such as that posited above in which there is no identifiable group of shareholders holding a controlling interest in the company's voting stock). It is this alternative that comprises the core of the changes proposed here.

### **Proposed Changes**

Attached hereto as Exhibit A is a proposed revision of the Final Rules that addresses the stated regulatory purposes of the attribution and affiliation rules while at the same time comporting with the real life situation facing small publicly-traded companies.

The only new concept introduced in the proposal is the definition of "dispersed voting power," applicable only to publicly-traded corporations, and the addition of that status as an alternative to the "control group" requirement in the rules regarding eligibility to bid on the "entrepreneurs' blocks" and qualification as a "small business." With the rule structured as proposed in Exhibit A, companies (including publicly-traded corporations) that are in a position to identify a "control group" as contemplated by the Final Rules will continue to have the opportunity to do so, while companies with widespread voting share ownership and no controlling affiliates will be able to avoid having the revenues and assets of management and non-affiliate shareholders attributed to them for purposes of these size determinations.

Under the rules proposed here, a publicly-traded corporation will be deemed to have "dispersed voting power" if it possesses two attributes: (1) no person (including any "group" as that term is used in the Securities Exchange Act of 1934<sup>6</sup>) has the power to control the election of more than 15 % of the corporation's directors (*i.e.*, a maximum of approximately one out of seven), and (2) no person or group, other than the corporation's management, is in control of the corporation. Metricom believes a substantial number of publicly-traded small businesses that are worthy of the favorable treatment accorded "entrepreneurial businesses" or "small businesses" in the broadband PCS auction possess both of these attributes.

Under the proposal, a publicly-traded corporation with "dispersed voting power," when applying the \$125 million annual revenues/\$500 million total assets tests applicable to "entrepreneurial businesses" or the \$40 million annual revenues test applicable to "small businesses," would not be required to aggregate with its own revenues and assets the revenues and assets of the members of its management team or its non-affiliate shareholders.<sup>7</sup> The theory underlying this result is that (1) to the extent a publicly-traded corporation with "dispersed voting power" is controlled by any group, it is controlled by its management, (2) its management, individually or as a group, does not possess a controlling stock interest in the corporation, and

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<sup>6</sup>Section 13(d) and Section 13(g) of the Securities Exchange Act of 1934, 15 U.S.C. 78a et seq., as amended (the "Exchange Act"), state that "when two or more persons act as a partnership, limited partnership, syndicate, or other group for the purpose of acquiring, holding, or disposing of securities in an issuer, such syndicate or group shall be deemed a "person" and therefore are required to make the disclosures indicated in those subsections.

<sup>7</sup>This proposal addresses only the "control group" requirement and attribution/aggregation rules. It is important to note that in order to qualify for "entrepreneurial business" or "small business" status under the proposed rules, a publicly-traded corporation would still be required to satisfy all of the other requirements of the applicable rule.

(3) its non-affiliate shareholders, by reason of management control, do not control the corporation; therefore, the wealth of the individual members of management and non-affiliate shareholders is not relevant to a determination whether the corporation meets the applicable size requirements.

The theory of "control" underlying the proposal is consistent with and supported by the Final Rules which, in turn, are drawn from the comparable SBA rules. In defining "control", both sets of rules adopt the principle that "every business concern is considered to have one or more parties who directly or indirectly control or have the power to control it." 47 C.F.R. §24.720(l)(2)(i) and 13 C.F.R. §121.401(c)(1). Moreover, both sets of rules state: "Control can arise through management positions where a concern's voting stock is so widely distributed that no effective control can be established." 47 C.F.R. §24.720(l)(2)(iii) and 13 C.F.R. §121.401(c)(3). This principle is further supported by the comments of the SBA itself, which urges that, rather than any specific level of equity ownership, " . . . a more appropriate determinant of [control] of a designated entity is actual operational control of the business and the control must extend to decisions concerning capital expenditures." Comments of SBA Chief Counsel for Advocacy on the Notice of Proposed Rulemaking in the matter first named above, dated November 10, 1993, at p. 17.

Metricom believes the proposed definition of "dispersed voting power" in Exhibit A is sufficiently restrictive to exclude from its scope those corporations with respect to which attribution of shareholder revenues and assets would be appropriate for purposes of determining the entity's size. The absence of any person or group possessing the ability to control the election of more than 15% of the directors (a more precise test of voting power than percentage

ownership of voting stock, which may possess differential rights) and the absence of any other person or group having "control" of the corporation, as defined in the Final Rules, will provide adequate safeguards against the type of circumvention the attribution rules are designed to prevent.

In addition, the securities law provide a method for the Commission or interested members of the public to readily verify under the "dispersed voting power" test that the publicly traded applicant or licensee maintains its status and does not actually become controlled by an undisclosed affiliate or attributable investor after the license is issued. The federal securities laws provide, under Section 13 of the Exchange Act and the rules and regulations promulgated thereunder, that any holder of more than five percent of any class of publicly traded stock must regularly file certain publicly available disclosure statements with the Securities and Exchange Commission. As noted above, this requirement also applies to all entities acting as a group for purposes of acquiring, holding or disposing of securities. The long form disclosure statement, which must be filed after a holder or group acquires more than five percent of the shares of any class of stock registered under the Exchange Act, contains information about the identify and background of the holder or group, the class of equity securities obtained and the holder or group's beneficial ownership thereof, the source and amount of funds for the purchase of the stock, the purpose of the acquisition, and any contract, arrangements, understandings or relationships between the reporting person (including a group) and the issuing corporation, Section 13D or the Exchange Act. Thereafter, an annual short form disclosure statement requires five percent holders or groups to disclose information such as the identity and background of the reporting person or group and the class and beneficial ownership of the holder

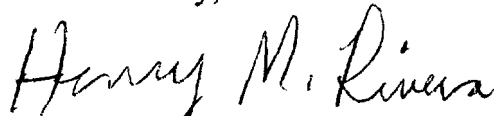
or group's securities. Section 13G of the Exchange Act.

In the absence of any controlling person or group, other than the individuals serving as collective directors and officers of the corporation, it follows naturally that the appropriate measure of the corporation's size (for purposes of the above-described size restrictions) is the revenues and assets of the corporation itself, including any affiliates it may control. In contrast to the case in which a "control group" of shareholders exists, where the anti-manipulative value of the attribution and aggregation rules is apparent, no regulatory purpose would be served by attributing to a corporation with "dispersed voting power" the assets or incomes (by analogy to "revenues") of the individual members of its management team or non-affiliate shareholders.

#### **Conclusion**

Based on the foregoing, Metricom respectfully suggests that the Commission, in furtherance of the Congressional mandate and objectives expressed in 47 U.S.C. §309(j)(4)(D) and the Commission's own objectives, and consistent with the comments of the SBA in this matter, should adopt the rule changes proposed herein. We will be calling you shortly for an appointment to review this letter and its proposals with you.

Sincerely,

A handwritten signature in cursive script that reads "Henry M. Rivera".

Henry M. Rivera  
Ginsburg, Feldman & Bress  
1250 Connecticut Avenue, N.W.  
Washington, D.C. 20036  
(202) 637-9012

Counsel for Metricom, Inc.

October 20, 1994

EXHIBIT A

PROPOSED REVISIONS TO BROADBAND PCS AUCTION RULES

§ 24.709 Eligibility for licenses for frequency Blocks C and F

. . . .

(b) Attribution and Aggregation of Gross Revenues, Total Assets, and Personal Net Worth.

. . . .

(4)(iii) The gross revenues, total assets and personal net worth of a person that holds an interest in the applicant (or licensee) shall not be considered for purposes of determining financial eligibility so long as (A) such person owns no more than 25 percent of the applicant's (or licensee's) total equity which shall include not more than 15 percent of the voting stock; (B) the applicant (or licensee) is a publicly traded corporation; and (C) the applicant (or licensee) has either (1) dispersed voting power or (2) an eligible control group that holds at least 50.1 percent of the voting stock, if a corporation, and at least 25 percent of the applicant's (or licensee's) equity.

. . . .

(e) Definitions. The terms *affiliate*, *business owned by members of minority groups and women*, *consortium of small businesses*, *control group*, *dispersed voting power*, *gross revenues*, *members of minority groups*, *passive equity*, *personal net worth*, *publicly traded corporation*, and *total assets* used in this section are defined in § 24.720.

. . . .

§ 24.720 Definitions.

. . . .

(b) Small Business; Consortium of Small Businesses.

(1) A *small business* is an entity that (i) together with its affiliates has average annual gross revenues that are not more than \$40 million for the preceding three calendar years; (ii) has no attributable investor or affiliate that has a personal net worth of \$40 million or more; (iii) either (A) is a publicly traded corporation with dispersed voting power or (B) has a control group all of whose members and affiliates are considered in determining whether the entity meets the \$40 million annual gross revenues and personal net worth standards; and (iv) such



control group (if applicable) holds 50.1 percent of the entity's voting interest, if a corporation, and at least 25 percent of the entity's equity on a fully diluted basis, except that a business owned by members of minority groups and/or women (as defined in subsection (c)) may also qualify as a small business if a control group that is 100 percent composed of members of minority groups and/or women holds 50.1 percent of the entity's total equity on a fully diluted basis and no single other investor holds more than 49.9 percent of passive equity in the entity. Ownership interests shall be calculated on a fully diluted basis; all agreement such as warrants, stock options and convertible debentures will generally be treated as if the rights thereunder already have been fully exercised, except that the such agreements may not be used to appear to terminate or divest ownership interests before they actually do so.

(2) For purposes of determining whether an entity meets the \$40 million gross revenues and \$40 million personal net worth standards in paragraph (1), gross revenues and personal net worth shall be attributed to the entity and aggregated as provided in § 24.709(b), ~~except that 24.709(b)(4)(iii) shall not apply.~~

. . . .

(n) Dispersed Voting Power. A publicly traded corporation has *dispersed voting power* if (1) no person (as such term is used in subsection (d) of §13 of the Securities Exchange Act of 1934, as amended (15 U.S.C §78m)) possesses, directly or indirectly, through the ownership of voting securities, by contract or otherwise, the power to control the election of more than 15 percent of the members of the board of directors or other governing body of such publicly traded corporation and (2) no person (as defined above), other than the management and members of the board of directors or other governing body of such publicly traded corporation in their capacities as such, directly or indirectly controls or has the power to control such publicly traded corporation.